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FISCAL IMPACT STATEMENT

LS 7683
BILL NUMBER: SB 501

NOTE PREPARED: Feb 5, 2007
BILL AMENDED:

SUBJECT: State Retirement Medical Benefits Account.

FIRST AUTHOR: Sen. Kenley
FIRST SPONSOR:

BILL STATUS: As Introduced

FUNDS AFFECTED: X GENERAL
X DEDICATED
X FEDERAL

IMPACT: State

Summary of Legislation: *Retirement Medical Benefits Account:* This bill establishes a retirement medical benefits account for elected officers, appointed officers, and employees of the executive, legislative, and judicial branches of state government to pay participants' medical expenses after retirement. The bill designates the Budget Agency as the account administrator.

Account Contributions: The bill requires the state to make annual contributions to the account based on the age of the participant. It provides for a supplemental contribution to the account for a participant who retires with at least: (1) 15 years of service with the state, for an employee; or (2) 10 years of service as an elected or appointed officer.

Account Benefits: The bill also provides that: (1) employees who qualify and have applied for a normal unreduced or disability retirement benefit at separation from service; and (2) elected or appointed officers with at least 10 years of service; are entitled to a benefit from the account. The bill allows the surviving spouse or dependent of a retired participant to receive a benefit. It also provides that unused amounts credited to a retired participant are forfeited if the retired participant dies without a surviving spouse or dependent.

State Budget Committee Oversight: The bill requires the Budget Committee to review the financial status of the account annually.

PERF Retirement Medical Benefits Account: The bill also provides that, if allowed by the Internal Revenue Service, the retirement medical benefits account established by the Public Employees' Retirement Fund (PERF) must: (1) require a state employee to convert certain unused vacation leave to a monetary contribution to the account at retirement; and (2) allow the state to contribute to the account on the employee's behalf an amount not to exceed two times the amount of the employee's contribution.

Effective Date: Upon passage; July 1, 2007.

Explanation of State Expenditures: *Summary:* This bill involves two programs established for the purpose of providing a source of payment for insurance premiums and for sickness, accident, hospitalization, and medical expenses upon the retirement of a state employee. The bill establishes the Retirement Medical Benefits Account into which the state makes "regular" contributions to employees based on age, and a "bonus" contribution upon normal, unreduced retirement based on years of service and provided through June 30, 2017. The bill also provides for the mandatory conversion of up to 30 days of unused vacation leave upon retirement (either full or early retirement with a reduced benefit) into a PERF-managed account, and the state would contribute twice the amount contributed by the employee.

Since the bonus contribution expires June 30, 2017, the following table provides cost estimates through FY 2018, the year after the bonus contribution requirement expires.

	Retirement Medical Benefits Account				PERF-Managed Account	
FY	Regular Contrib.	Reverted Contrib. **	Bonus Contrib.	State Admin ***	Leave Conversion Payments	Net State Contributions *
2008	$52.0 M	($6.9 M)	$20.7 M	6.6 M	$3.9 M	**$76.3 M**
2009	$52.0 M	(8.7 M)	20.7 M	1.2 M	4.0 M	**69.2 M**
2010	$52.0 M	(10.2 M)	20.7 M	-	4.1 M	**66.6 M**
2011	$52.0 M	(11.4 M)	20.7 M	-	4.1 M	**65.4 M**
2012	$52.0 M	(12.9 M)	20.7 M	-	4.2 M	**64.0 M**
2013	$52.0 M	(14.6 M)	20.7 M	-	4.3 M	**62.4 M**
2014	$52.0 M	(16.4 M)	20.7 M	-	4.4 M	**60.7 M**
2015	$52.0 M	(18.1 M)	20.7 M	-	4.5 M	**59.1 M**
2016	$52.0 M	(19.9 M)	20.7 M	-	4.6 M	**57.4 M**
2017	$52.0 M	(21.9 M)	20.7 M	-	4.8 M	**55.6 M**
2018	$52.0 M	(24.1 M)	-	-	4.9 M	**32.8 M**

* The amounts to be contributed from the state General Fund are assumed to represent approximately 55% of the state contributions listed above, with the balance, or 45%, to be contributed by various dedicated funds.
** Reverted amounts include only estimates for employees separating from state employment prior to retirement. Amounts that may revert due to the death after retirement of retired employees or their spouses are not estimated.
*** PERF estimates the administrative costs to be $2.0 M in one-time expenditures plus $8.2 M annually thereafter. Administrative costs are to be paid out of earnings on the contributions before being credited to the employees' subaccounts. Because the administrative costs are greater than total earnings initially, the state is assumed to pick up the balance until earnings exceed administrative expenditures.

Note: The estimated contributions required by the state do not factor in any potential behavioral changes that may occur in the retirement decisions of employees as a result of these additional benefits.

Background Information -

Retirement Medical Benefits Account: The bill establishes the Retirement Medical Benefits Account, which is a defined contribution account for the purpose of providing a source of payment for insurance premiums upon the retirement of an employee. If the State Budget Agency, administrator of the program, requests and receives an appropriate ruling from the Internal Revenue Service (IRS), the Account proceeds may be used for premiums for non-insurance health policies or for sickness, accident, hospitalization, and medical expenses.

Participants in the Account include employees of the executive, legislative, or judicial branches of state government; state elected or appointed officers; members of the General Assembly; and magistrates, juvenile court magistrates, and prosecuting attorneys.

Account Contributions: Regular, ongoing contributions are to consist of annual state payments made to employee subaccounts based on the age of the employee on the schedule provided in the following table.

Employee's Age in Years	Annual State Contributions
Less than 30	$500
At Least 30, Less Than 40	$1,000
At Least 40, Less Than 50	$1,500
At Least 50	$2,000

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The annual state contribution total is estimated to be approximately $52.0 M. The source of state contributions are approximately 55% from the state General Fund with the balance, or 45%, coming from various dedicated funds. This proportion applies to all state contributions described in this bill.

A bonus contribution is to be made upon a participant's retirement with normal unreduced benefits if the retirement occurs between July 1, 2007, and July 1, 2017, and the retiree on the last day of service has completed at least 15 years of service. The amount of the bonus contribution is to equal the number of years of service multiplied by $1,500. Bonus contributions are estimated to total approximately $20.7 M annually.

Upon the death or separation from service of an employee prior to retirement, the accumulated funds (both contributions and earnings) revert to the state. A preliminary estimate is that the reversions to the account will be approximately $6.9 M in FY 2008 and will grow to about $24.1 M in FY 2018. The reversions grow over time as individuals who die or separate from state employment prior to retirement have a longer history of state contributions and earnings into their individual subaccounts. [Note: The reversion estimates do not include estimates for reversions of unspent dollars upon the death of a retired employee or spouse.]

Personnel from the Public Employees Retirement Fund (PERF) estimate the cost to administer this program to be $2.0 M in one-time startup costs plus $8.2 M annually thereafter. The bill specifies that the administrative costs of the account are to be paid from the earnings of the account before the earnings are credited to the employees' subaccounts. An average annual earnings rate of 7.25% is assumed, based on assumptions used by PERF in their retirement fund valuations. Because the total earnings from the contributions are less than the total administrative expenditures initially, the amount of administrative expenditures in excess of earnings are assumed to be picked up by the state. The annual state share of the administrative expenses are estimated to be $6.6 in FY 2008 and $1.2 M in FY 2009, after which total earnings on contributions are estimated to exceed administration costs.

This analysis does not factor in potential behavioral changes in the timing of retirement decisions which may occur as a result of the increased retirement benefit. To the extent that the added benefits provide an incentive for earlier retirements than would otherwise occur, there could be some offsetting personnel expenditure reductions from hiring replacement employees at lower, entry-level wages.

Account Benefits: The bill provides that benefits are available to an employee upon separation from service and who qualifies and has applied for a normal, unreduced or disability retirement benefit. Benefits include the regular and bonus contributions made by the state plus any earnings on the money in the account (less administrative expenses). Currently, state employees may retire with normal, unreduced retirement benefits if the employee's (1) age is at least 65 and has accumulated at least 10 years of creditable service; (2) age is at least 60 and has accumulated at least 15 years of creditable service; or (3) age is at least 55 and whose age plus years of creditable service sum to at least 85 ("Rule of 85").

PERF Retirement Medical Benefits Account: The bill also provides for an additional contribution made to an existing retirement medical benefits account administered by PERF. To the extent permitted by the IRS, employees upon retirement will be required to convert to a monetary contribution the amount of accrued and unused vacation leave up to a maximum of 30 days times the value of the individual's salary; and the state will contribute an additional amount equal to twice the amount contributed by the retiring employee. This account is for the purpose of funding on a pretax basis benefits for the payment of sickness, accident, hospitalization, and medical expenses for the employee and the spouse and dependents of the employee after retirement. The additional contributions paid by the state are estimated to be approximately $3.9 M in FY 2008 and will grow each year based on the average state employee salary growth. [Note: This benefit is provided to employees who retire early with reduced benefits, as well as to those who retire with normal, unreduced benefits. An employee may retire with reduced retirement benefits if the employee's age is at least 50 with at least 15 years of creditable service.]

Data: Estimates of total contributions are based on data received from the State Budget Agency on the age distribution of 34,227 state employees. Estimates on the amounts of bonus contributions upon retirement and the amounts reverted by employees separating from state employment prior to retirement are based on age and years of service data received from PERF for individuals separating from state employment between January 1, 2002, and December 31, 2006. Estimates for the cost of the leave conversion provision are based on State Auditor data for actual cash payments for up to 30 days of unused vacation leave made to employees who separated from state service during CY 2006.

Explanation of State Revenues:

Explanation of Local Expenditures:

Explanation of Local Revenues:

State Agencies Affected: All.

Local Agencies Affected:

Information Sources: State Budget Agency; State Auditor data; Andrea Unzicker, General Counsel, PERF, 317-233-4132.

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